

1
2
3 **So Ordered.**



Patricia C. Williams
Patricia C. Williams
Bankruptcy Judge

4 **Dated: April 1st, 2013**
5
6
7

8 UNITED STATES BANKRUPTCY COURT
9 EASTERN DISTRICT OF WASHINGTON

10 In re:

11 LLS AMERICA, LLC,

12 Debtor.

No. 09-06194-PCW11

13 _____
14 BRUCE P. KRIEGMAN, solely in
15 his capacity as court-appointed
Chapter 11 Trustee for LLS America,
LLC,

16 Plaintiff,

Adv. No. 11-80127-PCW11

17 vs.

18 KEN PHILLIPS,

19 Defendant.
20 _____

MEMORANDUM DECISION RE:
DEFENDANT'S MOTION FOR
SUMMARY JUDGMENT (ECF NO. 21)

21 The adversary complaint was filed July 16, 2011, by the trustee of the LLS
22 America, LLC (hereinafter "LLS") bankruptcy estate and Ken Phillips was named as the
23 sole defendant. The complaint alleges that LLS engaged in a Ponzi scheme and that the
24 defendant was one of many "investors" (sometimes referred to as "lenders") who
25 provided funds to LLS in exchange for promissory notes. The defendant then received
26 distributions of funds from LLS. LLS filed a chapter 11 bankruptcy on July 21, 2009 in
27 the District of Nevada. The LLS bankruptcy was transferred to this court on
28 November 4, 2009. The complaint seeks return of all funds received by the defendant

MEMORANDUM DECISION RE: . . . - Page 1

1 under RCW 19.40 and .41, as well as pursuant to 11 U.S.C. §§ 544, 548, 550 and 551
2 of the Bankruptcy Code. This adversary is one of hundreds brought by the trustee, which
3 allege the same causes of action and attempt to recover from other defendants who
4 received distributions from LLS.

5 On December 31, 2012, the defendant requested summary judgment and the
6 dismissal of all claims. The grounds for the motion are: 1) lack of jurisdiction over the
7 defendant, who is a resident of Canada; 2) that United States law does not apply to this
8 controversy; and 3) that the plaintiff's accounting is incorrect and that the defendant did
9 not receive any distributions. The background of this controversy and much of the legal
10 analysis applicable to the present issues are set forth in a prior decision entered July 2,
11 2012 (ECF No. 146) in adversary proceeding No. 11-80093-PCW11, and will not be
12 repeated herein.

13 **JURISDICTION**

14 The defendant is a resident of British Columbia, Canada, as is the corporation
15 Dr. Ken Phillips, Inc. (hereinafter "the corporation"), discussed throughout this decision.
16 The declaration of Jane Phillips (ECF No. 24), the wife of the defendant, states that the
17 defendant is a dentist practicing in British Columbia, that the corporation operates a
18 dental practice in British Columbia, and that neither conduct business in the United
19 States.

20 In this case, it is not disputed that there were numerous relevant transactions over
21 the course of many years with transfers of funds to and from LLS.¹ The declaration of
22 Jane Phillips states that "at least" \$310,000 was transferred by the corporation to various
23 Canadian entities, which were substantially consolidated into the LLS bankruptcy estate.
24 The accounting reconciliation submitted by the trustee refers to over 100 transactions
25 between LLS and the defendant and/or the corporation. Numerous e-mails were sent by
26 Jane Phillips to LLS, and LLS sent numerous e-mail communications to investors such

27 ¹LLS refers to the various entities which compose the bankruptcy estate and the
28 estate itself.

1 as the defendant.

2 The defendant filed a proof of claim for \$420,000 in the LLS bankruptcy
3 proceeding on August 28, 2009 (Claim No. 49).² The defendant, through counsel, filed
4 a motion to withdraw the reference of this adversary proceeding to the district court.

5 Based upon the reasoning and additional facts set forth in the previous decision
6 entered in adversary proceeding No. 11-80093-PCW11 (ECF No. 146), the conclusion
7 is that jurisdiction exists. The defendant's request to dismiss for lack of jurisdiction is
8 denied.

9 CANADIAN LAW APPLIES

10 The defendant argues that since the defendant and/or the corporation dealt only
11 with Canadian entities, Canadian law applies to this adversary. Those Canadian entities
12 were substantially consolidated with the debtor LLS by memorandum decision and order
13 entered on September 8, 2011, in the underlying bankruptcy proceeding No. 09-06192-
14 PCW11 (ECF Nos. 770 and 771, respectively). That substantial consolidation was nunc
15 pro tunc, meaning that it relates back to the date of the filing of the bankruptcy petition.³

16 Plaintiff and the defendant agree that substantive consolidation has the effect of
17 consolidating assets and liabilities of the companies subject to consolidation. Defendant
18 asserts that the day before the court entered the substantive consolidation order, each of
19 the separate entities that are now consolidated possessed its own set of assets and
20 liabilities, and that although those Canadian entities might have had fraudulent transfer
21 claims under Canadian law, none of those companies were yet subject to the court's
22 substantive consolidation order and therefore, there were no fraudulent transfer actions
23 under United States law. The essence of the argument seems to be that the effect of

24
25 ²The defendant now offers to withdraw the proof of claim. Rule 3006 requires a
26 motion to that effect. Also, withdrawal has no effect upon jurisdiction. In re EXDS, Inc.,
301 B.R. 436 (Bankr. D. Del. 2003).

27 ³The Bankruptcy Appellate Panel affirmed the bankruptcy court's decision (ECF
28 No. 1133).

1 substantive consolidation was that any Canadian law cause of action possessed by the
2 Canadian entities became part of the LLS bankruptcy estate, but Canadian law continues
3 to apply to those causes of action. Those causes of action, assuming they exist, are not
4 being pursued in this adversary.

5 The plaintiff's claim to recover transfers under 11 U.S.C. §§ 544, 548, 550 and
6 551 arise under the Bankruptcy Code. Those claims are assets of the bankruptcy estate
7 and can only be brought by the court-appointed trustee for the estate. Defendant has
8 cited no authority for the proposition that claims arising under the Bankruptcy Code are
9 governed by Canadian law.

10 Choice of law issues were addressed in the previous decision entered July 2, 2012,
11 in adversary proceeding No. 11-80093-PCW11 (ECF No. 146). Not every transaction
12 which has a foreign element constitutes the extraterritorial application of law. Jay L.
13 Westbrook, The Lessons of Maxwell Communication, 64 Fordham L. Rev. 2531 (1996).
14 Courts must look at the facts of each case to determine whether or not the center of
15 gravity of the transaction exists outside the United States. In re Pacat Fin. Corp., 295 F.
16 394, 401 (D.C.N.Y. 1923).⁴ As held in the prior decision, the locus of this series of
17 transactions was in Spokane, Washington. The defendant's request to apply Canadian
18 law to this controversy is denied.

20
21 ⁴In its Order Granting Trustee's Motion for Substantive Consolidation and
Denying Oral Motions to Strike, ECF No. 771 filed September 8, 2011, in case No. 09-
06194-PCW11, this court held as follows on p. 15:

22 4. The LLS America Companies are substantively consolidated with the Debtor
23 nunc pro tunc effective as of July 21, 2009 (the date of the LLS America, LLC
bankruptcy filing).

24 5. The assets and liabilities of the LLS America Companies are hereby pooled
25 with the assets and liabilities of LLS America, LLC, the Debtor herein, and shall
26 be administered by the Chapter 11 Trustee for the benefit of the creditors of LLS
America, LLC and the LLS America Companies.

27 6. The trustee avoidance powers pursuant to 11 U.S.C. §§ 544, 547, 548, 549 and
28 otherwise, are preserved.

THE TRUSTEE'S ACCOUNTING IS INCORRECT
AND THE DEFENDANT RECEIVED NO TRANSFERS

The declaration of Jane Phillips (ECF No. 24) states that the defendant Dr. Ken Phillips never received any transfers from any of the LLS entities and further, that the corporation is the entity which received the transfers from the Canadian entities, which were substantially consolidated into the bankruptcy estate. To support the statement that all funds provided LLS were from the corporation, the declaration attached copies of checks variously dated between 2001 and 2004, payable to certain of those Canadian entities and drawn upon an account held by the corporation. Also attached are records of wire transfers dated in 2004 and 2005, which refer to "Dr. Ken Phillips" or to "Dr. Ken Phillips, Inc.," as sender, with the recipient listed as "Little Loans." The records reveal 19 transactions totaling approximately \$220,000. The plaintiff disputes the accuracy of the defendant's statement that the corporation transferred at least \$310,000 to LLS and the accuracy of the records produced.

The proof of claim filed in the name of the defendant attached the following promissory notes:

1. Note dated July 23, 2001 (typed date July 25, 2001), payable to the corporation in the amount of \$5,000 and payable by The Little Loan Shoppe, Ltd.
2. Note dated November 1, 2002, payable to the corporation in the amount of \$15,000 and payable by Little Loan Shoppe, Ltd.
3. Note dated May 7, 2003, payable to Dr. Ken Phillips in the amount of \$10,000 and payable by Little Loan Shoppe, Ltd.
4. Note dated August 16, 2004, payable to Dr. Ken Phillips in the amount of \$20,000 and payable by 639504 B.C., Ltd. and/or Little Loan Shoppe America and/or Doris E. Nelson.
5. Note signed October 6, 2006 (typed date September 20, 2006), payable to Dr. Ken Phillips in the amount of \$115,000 and payable by 0738116 B.C., Ltd.
6. Note signed July 17, 2007 (typed date December 15, 2006) payable to Dr.

1 Ken Phillips in the amount of \$300,000 and payable by 0738126 B.C., Ltd.

2 The last note states that “ALL PROMISSORY NOTES EXECUTED PRIOR TO
3 THE ABOVE DATE ARE CANCELLED AND THIS NOTE AND ITS TERMS
4 SHALL CONTROL THE PAYMENT OF ALL FUNDS PRESENTLY DUE THE
5 PAYEE.”

6 The declaration of Curtis Frye (ECF No. 33) submitted by the trustee states that
7 LLS frequently received instructions from investors to make payments under the
8 promissory notes to third parties. It attaches a 2006 e-mail from Jane Phillips, which
9 discusses “deposits” made by LLS and attaches a voided check from the corporation
10 account, but which does not expressly direct distributions be made to the corporation.
11 The accounting reconciliation attached to the Frye declaration refers to an account as
12 “Phillips, Dr. Ken or Jane” and in another column refers to the account as “Split -
13 Phillips-Dr. Ken Phillips, Inc.” The reconciliation then purports to be an accounting by
14 date and amount of all deposits made to the Phillips account and all transfers from the
15 account. It demonstrates deposits in the amount of \$250,000 and distributions of
16 \$354,725.08. Also attached are eight checks drawn by LLS and payable to Ken Phillips
17 or Jane Phillips which total \$21,903.31. Also attached are what appear to be unrelated
18 “check stubs” totaling \$3,340.00, but it cannot be determined if those represent
19 additional transfers. This contradicts the statement by the defendant that no funds were
20 transferred to the defendant, but implies that other funds were transferred to the
21 corporation, but it is unknown if that occurred at the request of the defendant.

22 There are contradictions and inconsistencies in the evidence. The declaration of
23 Jane Phillips attaches bank statements for the period of January 6, 2006 through
24 September 6, 2006, for the corporate account. Certain entries appear as “SPECIAL
25 DEPOSIT.” The source of the “special deposits” is not described in the Declaration, but
26 they are allegedly transfers from LLS to the corporation. However, there is a “special
27 deposit” in the amount of \$15,000 dated February 20, 2006, but the reconciliation
28 submitted by the trustee shows only one transfer in February, 2006, and that was in the

1 amount of \$6,167. The checks attached to the declaration of Jane Phillips (ECF No. 24)
2 drawn on the corporate account include a check dated January 31, 2004, in the amount
3 of \$20,000 and payable to Little Loan Shoppe. However, the trustee's reconciliation
4 reveals no transfers made to the Phillips' account in January, February or March of 2004.

5 Clearly, there are disputed facts as to the total amount transferred to LLS and
6 whether the transfers were from the defendant and/or the corporation. Clearly, there are
7 disputed facts as to the amount transferred from LLS to the defendant and/or the
8 corporation. There are disputed facts as to the role the corporation played in the transfers
9 to and from LLS. As there are disputed facts, the motion for summary judgment must be
10 denied.

11 CONCLUSION

12 Summary judgment is inappropriate and the defendant's motion for summary
13 judgment is be **DENIED**.